43rd ANNUAL REPORT

SASKATCHEWAN FOREST PRODUCTS CORPORATION

YEAR ENDED OCTOBER 31, 1987

Regina, Saskatchewan
February 18, 1988

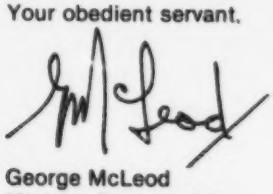
To His Honour,
The Honourable Frederick W. Johnson
Lieutenant Governor of the Province of Saskatchewan

Sir:

I have the honour to submit herewith the annual report of Saskatchewan Forest Products Corporation for the year ended October 31, 1987 including the financial statements therefore, duly certified by the Corporation's auditors and in the form approved by the Treasury Board, all in accordance with The Crown Corporations Act, 1978.

I have the honour to be, Sir,

Your obedient servant,



George McLeod
Minister Responsible,
Saskatchewan Forest
Products Corporation

Board of Directors

Mr. Pat Hill, Chairman of the Board, Saskatoon

Honourable George McLeod, Vice Chairman, Regina

Mr. Harvey Berg, Weekes

Mr. Armand Quessy, Debden

Mr. Alfred Sauder, Carrot River

Mr. Arnold Foss, Pierceland

Mr. Y. Don Elliott, Christopher Lake

Secretary to the Board

Mr. Ronald J. Kruzeniski, Regina

Corporation Officers and Management

Mr. Douglas Barclay	General Manager
Mr. Fred Hachey	Controller
Mr. Dale Vizina	Woodlands Manager
Mr. Henry A. Peters	Marketing Manager

Division Management

Mr. Roland St. Louis	Manager, Carrot River Sawmill
Vacant	Hudson Bay Plywood
Mr. Ken Wall	Manager, Treatment Plant, Prince Albert

Report of the General Manager

1987 was another very good year for forestry related products. Continued strong demand for lumber and plywood pushed prices up slightly from 1986 levels.

Market conditions for dimension lumber during 1987 remained positive with the U.S. market using a record 50 billion board feet of softwood lumber.

Because 98% of our sales were made in Canada the 15% surtax imposed on lumber exported to the U.S.A. had little effect on lumber sales.

Capital expenditures and major maintenance carried out during the year increased the efficiency at the mills particularly the Plywood Plant where green veneer recovery from peelers was increased and drying of veneer was improved.

Treated Wood products total sales were marginally higher than in 1986. Outdoor wood sales was the major contributor to the increased sales.

Outlook

A predicted decline in the 1988 housing starts should be offset by increased residential repairs and alterations. Foreign consumption of Canadian and U.S. wood should remain stable and if the line on interest rates continues at a reasonable level then prices should remain constant in 1988.

Prices are expected to decline in the first quarter and then increase to 1987 levels. Treatment Plant operations will be significantly reduced in 1988.

Financial

Consolidated earnings for the year after a write-down of notes and interest receivable of $1.4 million and a loss of $1.0 million by subsidiary Northern Forest Operations Ltd. was $606 thousand.

Lumber sales volumes were down significantly from 1986 levels when two sawmills were operating as compared to one in 1987. Total sales revenue was $34.1 million in 1987, $9.5 million less than in 1986.

Total capital expenditures for the year were $956.0 thousand.

Long term debt was reduced by $1.9 million to $3.1 million. Interest expense was $2.0 million in 1987 as compared to $3.1 million in 1986. Reduced interest expense was a result of applying proceeds from sale of Big River Sawmill to long term debt.

Report On Operations

Woodlands

Logging activities during 1987 were very successful, due mainly to a better pulpwood market and a higher than average temperatures.

Jack Pine power pole production continued at approximately the same level as in past years. Most Most of the raw materials were purchased from Wyerhaeuser and other small producers in Saskatchewan. Saskatchewan Forest Products Corporation also purchased larger class material from out of province.

Post production was reduced approximately 30% from 1986 due mainly to poor markets.

Harvesting of Spruce Budworm infested timber remains a high priority in the Carrot River area, with approximately 90% of the Sawmill requirement salvage from infested stands.

Several reforestation projects were completed in the Carrot River - Prince Albert areas in co-operation with the Canadian Forestry Service. Present plans are to continue these very high priority silvicultural projects in 1988.

Saskatchewan Forest Products Corporation's safety incentive program for Logging Operations was continued in 1987 with a high degree of success.

Carrot River Sawmill

The mill operated 263 days with one shift per day and produced 23,549 MFBM. Average daily lumber production was 90 MFBM. Planermill production was 24,911 MFBM for an average daily production of 102 MFBM. The mill employed an average of 66 hourly employees at total payroll cost of $2.0 million.

Hudson Bay Plywood

The green veneer and press departments operated on a 2 shift basis, 5 days a week while the dryers operated on a 3 shift basis, 5 days a week. Total plywood production was 80,069 m3/8 which was an increase of 4% from 1986 and is attributed to increased yield from peelers. The mill employed an average of 197 hourly employees and 14 salaried employees. The payroll for 1987 was $6.3 million.

Treatment Plant

Production of all products was considerably reduced in 1987. A decison was made to discontinue outdoor wood since we were unable to complete successfully against eastern manufacturers where the majority of our product is sold. The plant employed an average of 33 hourly employees and total payroll was $1.1 million.

Northern Forest Operations Ltd. (a subsidiary)

The La Ronge Sawmill and inventories were sold in June 1987 and the Green Lake Sawmill and Meadow Lake Planer Mill were sold in September 1987 leaving the Weyakwin Log Home Manufacturing Plant as the only mill left with Northern Forest Operations. The Weyakwin Mill has been offered for sale but attempts by potential purchasers to raise the necessary funding has been unsuccessful.

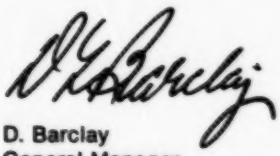
Northern Forest Operations incurred an operating loss of $734,064 in 1987 and a loss on sale of assets and inventories of $281,600 for a total of $1,015,664.

Personnel

In 1987 the total number of employees on the active payroll at year-end had increased to 355, a slight increase over the 1986 level of 30.

Union and Management personnel attended various training seminars during the year.

There were no major labour problems in 1987 and it is felt that Union/Management relations have improved during the year.



D. Barclay
General Manager
Saskatchewan Forest Products Corporation

AUDITORS' REPORT

To the Members of the Legislative
Assembly of the Province of Saskatchewan

We have examined the consolidated statement of financial position of Saskatchewan Forest Products Corporation as at October 31, 1987 and the consolidated statements of earnings and deficit and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the corporation as at October 31, 1987 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Price Waterhouse

Saskatoon, Saskatchewan
December 4, 1987

Price Waterhouse
Chartered Accountants

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

	Note Reference	October 31 1987	October 31 1986
		(In Thousands)	
ASSETS			
Current assets:			
Cash on deposit		$ 1,666	$ 67
Accounts receivable		4,221	3,926
Prepaid expenses		195	250
Inventories	1	4,958	8,430
		11,040	12,673
Investments	1 & 3	5	42
Property, plant and equipment	1 & 4	9,818	9,844
		$20,863	$22,559
LIABILITIES AND PROVINCE'S EQUITY			
Current liabilities:			
Accounts payable and accrued		$ 2,027	$ 2,444
Short-term loans	5	14,099	14,049
Current portion of long-term notes	6	1,283	1,283
		17,409	17,776
Long-term notes, less current portion	6	3,129	5,064
Province of Saskatchewan's equity:			
Equity advances from Crown Investments Corporation of Saskatchewan	7	20,112	20,112
Deficit		19,787	20,393
		325	(281)
		$20,863	$22,559

(See accompanying notes)

CONSOLIDATED STATEMENT OF EARNINGS AND DEFICIT

	Note Reference	Year Ended October 31 1987	1986
		(In Thousands)	
Revenue:			
Sales of forest products		$34,120	$43,568
Expenses:			
Operating costs		29,976	36,229
Selling, general and administrative		1,147	1,276
Depreciation and amortization	1	779	1,152
Interest on long-term notes	6	595	1,445
Other interest		1,387	1,696
		33,884	41,798
Earnings before extraordinary items		236	1,770
Extraordinary items	8	370	(652)
Net earnings for the year		606	1,118
Deficit, beginning of year		20,393	21,511
Deficit, end of year		$19,787	$20,393

(See accompanying notes)

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

	Note Reference	Year Ended October 31 1987	1986
		(In Thousands)	
Cash provided by (used in) operating activities:			
Earnings before extraordinary items		$ 236	$ 1,770
Add charges to operations not requiring a current cash payment -			
Depreciation and amortization	1	779	1,152
Loss (gain) on sale of property, plant and equipment (before extraordinary item)		7	(20)
		1,022	2,902
Net change in non-cash working capital balances related to operations	12	1,523	(1,598)
Cash provided by operating activities		2,545	1,304
Cash provided by (used in) investment activities:			
Compensation for shortfall incurred on sale of operating assets of Big River sawmill	8	652	—
Proceeds from sale of Northern Forest Operations Ltd. sawmill operations	8	1,311	—
Proceeds from sale of property, plant and equipment (before extraordinary item)		4	43
Proceeds of assignment of income debenture regarding disposition of Big River sawmill	8	—	8,000
Additions to property, plant and equipment	1 & 4	(1,015)	(1,315)
Decrease in advances to joint venture		37	75
Cash provided by investment activities		989	6,803
Cash used in financing activities:			
Reduction of long-term notes	6	(1,935)	(9,284)
Cash used in financing activities		(1,935)	(9,284)
Net increase (decrease) in cash during the year		1,599	(1,177)
Cash on deposit, beginning of year		67	1,244
Cash on deposit, end of year		$ 1,666	$ 67

(See accompanying notes)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
OCTOBER 31, 1987

1. Summary of accounting policies:

This summary of significant accounting policies is a description of the accounting methods and practices that have been used in the preparation of these consolidated financial statements.

Consolidation principles —

These consolidated financial statements include the accounts of the company's wholly-owned subsidiary, Northern Forest Operations Ltd.

Inventories —

Inventories of logs and mill supplies are valued at the lower of cost and replacement cost. Inventories of lumber, plywood and treated products are valued at the lower of average cost and new realizable value. Average cost includes appropriate production overheads.

Investments —

The corporation's investment in co-operatives is recorded at cost with dividents being reflected in earnings when received. The investment in the joint venture is recorded at net realizable value.

Property, plant and equipment —

The costs of maintenance, repairs and minor renewals or replacements are charged to operations as they arise. The cost of major replacements, extensions and improvements are capitalized in the property, plant and equipment accounts. Government grants received in connection with the construction or expansion of production facilities are credited to the cost of such assets. On retirement or disposition of property, plant and equipment, the costs thereof and the related accumulated depreciation are eliminated from the accounts and any gains or losses are reflected in the statement of operations.

Property, plant and equipment are stated at cost and are depreciated over their estimated useful lives primarily on the diminishing-balance basis at the following rates:

Buildings	5 - 10%
Machinery and equipment	6.7 - 10%
Vehicles	15%
Site improvements	4%
Office equipment	10%
Roads	10%

2. Status of Saskatchewan Forest Products Corporation:

The corporation was established by Order-in-Council 1899 of 1949 and continues under the provisions of The Crown Corporations Act. These financial statements will be consolidated in the accounts of the Crown Investments Corporation of Saskatchewan.

3. Investments:

	October 31	
	1987	1986
	(In Thousands)	
Investment in and advances to joint venture	$	$ 37
Investment in co-operatives	5	5
	$ 5	$ 42

The corporation has a 51% interest in Western Overlay Industries, a joint venture. The venture has been inactive since 1982 and has now liquidated and distributed all of its assets.

4. Property, plant and equipment:

	October 31 1987	October 31 1986
	(In Thousands)	
Land	$ 724	$ 672
Building and site improvements	4,173	4,413
Roads and spur tracks	392	391
Machinery and equipment	9,747	8,955
	15,036	14,431
Less: Accumulated depreciation	5,218	4,587
	$ 9,818	$ 9,844

5. Short-term loans:

The short-term loans are due to Crown Investments Corporation of Saskatchewan, bear interest at 9.95% (1986 - 8.9%) and mature December 31, 1987.

6. Long-term notes:

	October 31 1987	October 31 1986
	(In Thousands)	
Crown Investments Corporation of Saskatchewan 10% promissory note repayable in annual instalments of $83,400. Interest is only payable in years in which the corporation records net earnings.	$ 917	$ 1,000
Crown Investments Corporation of Saskatchewan promissory note, see below.	3,495	5,347
	4,412	6,347
Less: Portion due within one year classified as current	1,283	1,283
	$ 3,129	$ 5,064

Interest on this loan is negotiated November 1 annually. The interest rate over the past year was 10% (1986 - 10%). Principal repayments will be $1,200,000 on each October 31 until maturity with the final payment being $1,347,000. Principal may be repaid prior to maturity without penalty. Interest is due annually.

7. The Province of Saskatchewan's equity:

The Province of Saskatchewan's equity in the corporation is made up of equity advances by the Crown Investments Corporation of Saskatchewan to the corporation since its inception, less amounts repaid or forgiven. These advances are repayable at the discretion of the Crown Investments Corporation of Saskatchewan and do not bear interest. The deficit represents accumulated profits and losses of the corporation since the date of the reorganization on November 1, 1977.

8. Extraordinary items:

1987 -

During the year a related party agreed to compensate Saskatchewan Forest Products Corporation for the shortfall incurred in 1986 on the sale of the operating assets of the Big River sawmill to the Big River Lumber Corporation and assignment of the related income debenture to Prince Albert Pulp Company Ltd. A payment was received in the amount of $652,000 which has been included in current period earnings.

During 1987, the company's wholly-owned subsidiary, Northern Forest Operations Ltd., sold two of its three operating sawmills for total proceeds of $1,311,000. These mills had inventory with a book value of $1,342,000 and fixed assets with a net book value of $251,000. This resulted in a loss on the sale of these mills of $282,000.

	(In Thousands)
Compensation for shortfall incurred on 1986 sale of operating assets of Big River sawmill	$ 652
Loss on sale of Northern Forest Operations Ltd. sawmill operations	(282)
	$ 370

1986 -

On September 9, 1986, the operating assets of the Big River sawmill were sold to the Big River Lumber Corporation for total proceeds of $7,784,000. The carrying value of inventories and fixed assets was $8,652,000, resulting in a shortfall of $868,000. Saskatchewan Forest Products Corporation's interest in the proceeds of disposition was subsequently assigned to the Prince Albert Pulp Company Ltd. in exchange for an $8,000,000 reduction of the Crown Investments Corporation of Saskatchewan promissory note, resulting in a $216,000 gain.

	(In Thousands)
Shortfall on sale of Big River assets	$ 868
Gain on assignment of proceeds of disposition	(216)
Shortfall on sale of operating assets of Big River sawmill	$ 652

9. Contingencies:

Contingent liability —

Various lawsuits and claims are pending by and against the Corporation. It is the opinion of management that final determination of these claims will not materially affect the financial position or the results of operations of the company.

Contingent gains —

Pursuant to a purchase agreement between Northern Forest Operations Ltd. and the Province of Saskatchewan, the company may seek compensation from the Province for any losses arising from the operations subsequent to October 31, 1985. The agreement also entitles the company to reimbursement of all closedown costs, to a maximum of $500,000, relating to the closure of any or all of the purchased operations up to March 17, 1991 due to financial non-viability.

No provision has been made in the financial statements for any such compensation or reimbursement which may be recovered.

10. Related party transactions:

Included in these consolidated financial statements are income and expense amounts resulting from routine operating transactions conducted at prevailing market prices with various Saskatchewan Crown controlled departments, agencies and corporations with which the corporation is related.

Account balances resulting from these transactions are included in the consolidated statement of financial position and are settled on normal trade terms.

Other amounts due to related parties and the terms of settlement are described separately in the consolidated financial statements and the notes thereto.

11. Remuneration:

The corporation's directors received remuneration of $7,200 (1986 - $7,200) during the fiscal year. The senior officers received, in aggregate, remuneration of $174,000 for 1987 (1986 - $218,000).

12. Statement of changes in financial position:

The net change in non-cash working capital balances related to operations is comprised of the following:

	October 31	
	1987	1986
	(In Thousands)	
Cash provided by (used in) operating activities:		
Decrease (increase) in accounts receivable	$ (295)	$ 633
Decrease in prepaid expenses	55	28
Decrease (increase) in inventories of continuing operations	2,130	(521)
Increase (decrease) in accounts payable and accrued	(417)	139
Increase in short-term loans	50	849
(Decrease) in due to Province of Saskatchewan	—	(2,726)
Net change in non-cash working capital balances related to operations	$ 1,523	$ (1,598)